

NORTH LONDON WASTE AUTHORITY

REPORT TITLE

2004/05 THIRD BUDGET REVIEW AND 2005/06 BUDGET FORECAST

REPORT OF

FINANCIAL ADVISER

FOR SUBMISSION TO

DATE

AUTHORITY MEETING

15 DECEMBER 2004

1. SUMMARY OF REPORT

This report is the third in the current year of a series of regular reports on the Authority's finances. It concludes that the Authority is currently forecast to have a revenue surplus of £3.612m at 31 March 2005. A further assessment of the budget and resource requirements for the year ahead indicates that the 2005/06 net budget requirement is currently estimated to be £54.182m, which after use of forecast revenue balances of £3.612m, will require funding of £50.570m by constituent councils. This represents an increase of £5.420m (12.01%) over the costs to constituent councils in 2004/05. This figure is £1.544m (3.39%) lower than previously forecast. There remain a number of issues that need to be clarified and which could influence the final shape of the 2005/06 budget and levy. Further advice will be provided to Members at the budget meeting in February.

Members are also requested to consider the proposal to increase non-household charges in 2005/06 to reflect the opportunity cost to the Authority of landfilling biodegradable trade and commercial waste, and to introduce a scheme to reward boroughs that reduce the biodegradable fraction of their waste stream.

2. RECOMMENDATIONS

The Authority is requested to:-

- (i) Note the third review of the 2004/05 revenue budget.
- (ii) Note the current assessment of the budget and resource requirements for 2005/06.
- (iii) Comment on the proposals to increase non-household charges in 2005/06 to reflect the opportunity cost to the Authority of using LATS allowances for trade and commercial wastes, and to introduce a scheme to reward boroughs that reduce the biodegradable fraction of their waste stream.
- (iv) Note the issues that will need to be addressed at the budget and levy meeting on 9 February 2005.

Signed by the Financial Adviser:

Date:

3. **Review of the 2004/05 Revenue Budget**

- 3.1 At its meeting on 11 February 2004 the Authority agreed an original budget of £49.917m to be financed by estimated balances of £4.767m, charges to boroughs for non-household waste of £6.776m and a levy of £38.374m.
- 3.2 In subsequent reviews Members have been advised of the higher level of revenue balances brought forward from 2003/04 (- £1.313m), slippage of income from 2003/04 (- £0.350m), an increase in income arising from the investment of cash balances (- £0.110m) and an increase in costs arising from the Waste Strategy and Contracts staffing review (+ £0.100m).
- 3.3 At the October meeting Members were also advised of other possible budget pressures that could not be quantified at that time. The third review of the budget includes an assessment of these budget pressures and has identified a number of further variances, the net effect of which is estimated to increase the level of surplus revenue balances likely to be available at 31 March 2005 by £1.939m to £3.612m. Details of the most significant changes identified by the third review are shown below.
- 3.4 **Transport and Disposal (- £1.294m)**
- 3.4.1 In October Members were advised that based upon data available for the period April to August 2004 there had been a net reduction of 1.75% in the level of waste entering the residual waste stream over the same period in 2003/04. On this basis, the 2004/05 residual waste stream was estimated to reduce by 15,011 tonnes to 840,822 tonnes. Data now available for the period up to October 2004 indicates a net reduction of 2.42%. Allowing for a 1% increase in the waste stream for the remainder of the year, and current levels of recycling activity, the residual waste stream for the year could be in the region of 843,610 tonnes. The boroughs, however, have reported their intention to increase recycling activity during the second half of 2004/05. Based upon the boroughs' original estimates of their recycling activity in 2004/05 it is estimated that the residual waste stream could reduce by a further 32,153 tonnes by year-end. Allowing for the latter the 2004/05 residual waste stream is currently estimated to reduce to 815,677 tonnes. This compares with an original budget assumption of 819,823 tonnes.
- 3.4.2 Compared with the position reported in October all boroughs have experienced some downward movement in their waste streams. At one extreme, the Camden waste stream is currently forecast to increase by 0.53% for the year, whilst at the other, the Waltham Forest waste stream is currently forecast to reduce by 6.12%. Although it is clear that increased borough recycling activity is having a beneficial impact on the residual waste stream the figures also reveal that the underlying growth in the waste stream (before recycling) is increasing at 2.9% per annum (compared with a budget assumption of 2.5%).
- 3.4.3 Although there has been an overall increase of 2.9% in the underlying waste stream there has been a significant reduction in the civic amenity waste stream. Civic amenity waste tonnages are currently projected to reduce from c. 57,000 tonnes in 2003/04 to 44,000

tonnes in 2004/05. This compares with an original budget assumption of 64,500 tonnes. The latter assumed an increase in civic amenity tonnages arising from the new Islington civic amenity waste facility at Hornsey Street and also a new civic amenity facility planned by Waltham Forest. The latter is not now expected to materialise in the near future and the Islington civic amenity tonnages suggest that the new Hornsey Street facility is not yet attracting more civic amenity waste than Ashburton Grove.

- 3.4.4 The LondonWaste waste disposal contract is subject to an annual price review in December each year. The 2004/05 original budget assumed an inflation increase of 2.5% from this date, however, as the annual rate of increase in the Retail Price Index for the year to the end of October 2004 is 3.3% this could add c. £0.045m to costs in 2004/05 and £0.155m in a full year.
- 3.4.5 Allowing for these changes the costs of transport and disposal is estimated to reduce by £0.736m.
- 3.4.6 Details of the percentage movement in 2004/05 tonnage levels for each borough compared with the 2003/04 tonnages may be summarised as follows:-

		October Forecast (April to August)	December Forecast (April to October)	Variance
Barnet	-	- 1.38%	- 1.86%	- 0.48%
Camden	-	+ 0.90%	+ 0.53%	- 0.37%
Enfield	-	- 3.21%	- 3.32%	- 0.11%
Hackney	-	- 1.16%	- 1.28%	- 0.12%
Haringey	-	- 0.84%	- 2.17%	- 1.33%
Islington	-	- 1.33%	- 2.82%	- 1.49%
Waltham Forest	-	- 5.19%	- 6.12%	- 0.93%

- 3.4.7 The increase in recycling activity is having a significant effect on waste stream forecasts. Arrangements have been made with the boroughs for monthly recycling data to be made available to the Authority as soon as it is available. This information, together with tonnage data to be collected for November and December, will help inform the decisions which must be made on the 2004/05 revised budget and 2005/06 draft budget at the Authority meeting in February.
- 3.4.8 LondonWaste Ltd's Compensation Review claim for 2004/05 is now also expected to be lower than that assumed in the original budget. This is due to the increased price obtained by the Company for the sale of electricity during the current year and the reduction in incineration levels whilst the Company undertakes the WID refurbishment works at the Edmonton Energy-from-Waste (EfW) facility. (Under the Compensation Review clause the NLWA is required to contribute towards the reduction in electricity income – which had not

been priced for in the original contract price – as a result of the cessation of the Non Fossil Fuel Obligation in December 1998). This is estimated to result in a saving of £0.558m.

3.5 Fridges and Freezers (- £0.098m)

3.5.1 The original budget allowed for the treatment of 61,500 units at an average cost of £17.43 per appliance (the actual rate depends upon the treatment required and the delivery point). Based upon the current number of appliances entering the waste stream the full year forecast is estimated to reduce to c. 58,000 appliances at an average cost of £16.75 per appliance, i.e. a potential saving of £0.098m.

3.6 Landfill Tax (- £0.598m)

3.6.1 The original budget assumed a reduction in the quantities of bottom ash recycled by LondonWaste Ltd. Although, there had been the risk of some reduction in 2003/04 the Company has been able in the year to-date to maintain a recycling level of about 90%. This is expected to continue for the remainder of the year. LondonWaste Ltd's landfill tax claim for the year is therefore currently estimated to be c. £0.598m lower than originally estimated.

3.7 Legislative Review – Hazardous Waste (+ £0.911)

3.7.1 At the last meeting I advised that new rules to end the co-disposal of hazardous and non-hazardous waste came into force on 16 July 2004 and that the costs of transporting and disposal of hazardous waste looked set to rise. I also advised that the new requirements were likely to impact on the costs incurred by LondonWaste Ltd for the disposal of waste residues that arise from the incineration process (precipitator ash). LondonWaste Ltd has advised that since July 2004 the cost of disposal of this type of waste has risen from £41 to £110 per tonne and could rise to £150 per tonne when the full impact of the Hazardous Waste Regulations come into effect in July 2005. It is understood that LondonWaste Ltd is proposing to make a claim under the Legislative Review clause. Clearly, the merit of any claim will need to be assessed when it is received, however, on the figures provided by LondonWaste Ltd this could add c. £0.911m to the Authority's costs in 2004/05.

3.8 Hendon Transfer Station (- £0.031m)

3.8.1 The actual non-domestic rate charge for the year is lower than allowed for in the original budget.

3.9 Recycling Credits (- £0.097m)

3.9.1 Although 2004/05 is not a statutory target year the third review continues to assume that boroughs will succeed in achieving their original recycling and composting targets for 2004/05, i.e. a total of 151,893 tonnes excluding hardcore. Although hardcore recycling is outside the Government's statutory recycling targets the recycled waste is eligible to

receive a recycling credit payment. The budget therefore also allows for hardcore recycling of 9,000 tonnes.

3.9.2 Based upon information provided by the boroughs for the 6 month period to the end of September a total of 63,257 tonnes of waste has been recycled or composted. This compares favourably with the actual recycling activity achieved in 2003/04 of 88,455 tonnes. Assuming similar levels of activity in the second half of the year the boroughs should achieve a recycling/composting level of c. 124,000 tonnes in 2004/05. However, it is understood that boroughs are continuing to roll-out recycling initiatives across their respective borough areas and therefore there is a prospect of the boroughs exceeding this level and moving closer to their original 2004/05 recycling and composting targets. As the value of recycling credits paid by the Authority are determined by the Authority's most expensive disposal route it is necessary to ensure that this budget is sufficiently robust to meet the likely increase in borough recycling activity. This is achieved by allowing for recycling activity based upon the borough's original target assumptions.

3.9.3 The value of the estimated recycling credit payment for 2004/05 has reduced from £57.77 to £57.17. As a consequence the third review allows for a budget reduction of £0.097m.

3.10. **Waste Strategy and Contracts Group (- £0.074m)**

3.10.1 In view of the current vacancies and delays in implementing the staff review the third review allows for a reduction of £0.074m. Three posts are, however, currently being advertised, and a further three will be advertised in January 2005.

3.11 **Excess Creditor Provision (Previous Years) (- £0.896)**

3.11.1 As actual recycling activity by boroughs in 2003/04 has been lower than assumed in closing the 2003/04 accounts it will be possible to write back an excess creditor provision to revenue of £0.896m in 2004/05.

3.12 **Charges to Boroughs for Non-Household Waste (+ £ 0.209m)**

3.12.1 In view of the changes both in the volume and make-up of the waste stream non-household tonnages are currently estimated to reduce by 5,349 tonnes for the year. Charges are currently estimated to increase from £40.34 to £40.38 per tonne (higher than budgeted inflation). The overall effect of these changes is to reduce the estimated income from non-household charges by £0.209m for the year. The potential financial effect on boroughs varies.

3.12.2 Assuming boroughs continue to deliver waste at current levels the potential impact on individual boroughs is estimated to be as follows:-

	2004/05 Original Estimate £	2004/05 Current Forecast £	Estimated Variance £
Barnet	765,411	740,287	- 25,124
Camden	1,438,282	1,416,409	- 21,873
Enfield	568,955	541,254	- 27,701
Hackney	1,023,345	971,220	- 52,125
Haringey	940,164	913,355	- 26,809
Islington	1,140,130	1,118,647	- 21,483
Waltham Forest	900,026	865,868	- 34,158
	6,776,313	6,567,040	- 209,273

3.12.3 The figures currently indicate that all boroughs could be entitled to a refund.

3.13 Contingency

3.13.1 It would not be prudent, at this stage of the budget process to reduce the 2004/05 contingency provision (£0.500m). Further advice on this will be provided at the budget and levy meeting in February.

3.14 Overview

3.14.1 An assessment of the current financial position is summarised in Table 1 on the following page.

Table 1

	2004/05 Original Budget	2004/05 Second Review	2004/05 Third Review	Variance between 2nd & 3rd Reviews
	£'000	£'000	£'000	£'000
Expenditure				
Borough Waste (Ex. CA Waste)				
- Main Waste Disposal Contract	27,408	27,408	27,002	(406)
- Clinical Waste	184	184	200	16
Civic Amenity Waste	2,774	2,774	1,870	(904)
Fridges and Freezers	1,072	1,072	974	(98)
Landfill Tax	6,360	6,360	5,762	(598)
LWL Legislative Review – Hazardous Waste	0	0	911	911
Hendon Transfer Station	417	417	386	(31)
Hornsey Street Transfer Station	1,405	1,405	1,405	
Recycling Credits	9,295	9,295	9,198	(97)
Other Recycling Initiatives	100	100	100	
Agency Services	465	465	465	
Waste Strategy and Contracts Group	404	504	430	(74)
Annual Compensation	30	30	30	
Provision for possible Litigation Costs	50	50	50	
Contribution to Earmarked Reserve	20	20	50	30
Excess Creditor Provision (Previous Years)	<u>0</u>	<u>0</u>	<u>(896)</u>	<u>(896)</u>
	49,984	50,084	47,937	(2,147)
Less				
Income				
Rents	(77)	(77)	(78)	(1)
Interest on Balances	(490)	(950)	(950)	
Estimated Dividend Stream	<u>(0)</u>	<u>0</u>	<u>(0)</u>	<u>(1)</u>
	(567)	(1,027)	(1,028)	
Net Expenditure	49,417	49,057	46,909	(2,148)
Contingency	<u>500</u>	<u>500</u>	<u>500</u>	<u>(1)</u>
Total Net Expenditure 2004/05	<u>49,917</u>	<u>49,557</u>	<u>47,409</u>	<u>(2,148)</u>
Financed By :-				
Balances b/fwd	(4,767)	(6,080)	(6,080)	
Charges to Boroughs (Non-household waste) 2003/2004 Levy	(6,776)	(6,776)	(6,567)	209
	(38,374)	(38,374)	(38,374)	
Estimated Revenue Balances as at 31 March 2005 (Surplus)		(1,673)	(3,612)	(1,939)

4. **2005/06 Budget Forecast**

- 4.1 At the Authority meeting in July I provided Members with a further assessment of the budget and resource requirements for 2005/06. This indicated that the net budget requirements for the year ahead were estimated to be in the order of £53.677m. Allowing for the use of estimated revenue balances of £1.563m at 31 March 2005, the cost to constituent councils in 2005/06 was estimated to rise by £6.964m (15.4%) to £52.114m. This compared with an increase of 18.22% provided as an early forecast at the February meeting of the Authority. The reduction was due to the improvement in revenue balances at 31st March 2004.
- 4.2 Allowing for the estimated full year effect of known and potential changes the cost to constituent councils in 2005/06 is now estimated to rise by £5.420m (12.01%) to £50.570m. This represents a reduction of £1.544m (3.39%) over the July forecast and reflects the results of a detailed assessment of the potential costs of waste disposal in 2005/06.
- 4.3 Details of the 2005/06 budget forecast are summarised in Table 2 whilst further information on the budget forecast assumptions can be found at paragraph 5.

4.4 Table 2 provides a summary of the 2005/06 budget forecast:-

Table 2	2005/06 Budget Forecast £'000	
Borough Waste (Ex. CA Waste)		
- Main Waste Disposal Contract	27,135	
- Clinical Waste	222	
Civic Amenity Waste	1,904	
Fridges and Freezers	1,006	
Landfill Tax	6,663	
LWL Legislative Review – Hazardous Waste	1,668	
LWL Legislative Review – Edmonton Rating Review	47	
Hendon Transfer Station	405	
Hornsey Street transfer Station	1,965	
Recycling Credits	12,052	
Other Recycling Initiatives	100	
Agency Services	476	
Waste Strategy and Contracts Group	574	
Annual Compensation	30	
Provision for Possible Litigation Costs	50	
Contribution to Earmarked Reserve	<u>25</u>	
	54,322	
Less		
Income		
Rents	(80)	
Interest on Balances	(560)	
Estimated Dividend Stream	<u>(0)</u>	
	(640)	
Net Expenditure	53,682	
Contingency	<u>500</u>	
2005/06 Budget Forecast	54,182	
	=====	
To be financed by :-		
Estimated Balances b/fwd	(3,612)	
Charges to Boroughs (Non-household waste)	(7,397)	}
		} (50,570)
2005/06 Forecast Levy	(43,173)	}
		} (+ 12.01%)

5. **2005/06 Budget Assumptions**

5.1 The following factors have been taken into account:-

5.2 **Inflation**

5.2.1 A general allowance for inflation of 2.5%.

5.3 **Transport and disposal**

5.3.1 The transport and disposal budget has been based upon a total residual waste stream of 806,000 tonnes, i.e. a net reduction of 9,677 tonnes over the 2004/05 projected outturn. This reflects the requirement for boroughs to continue to make significant stepped changes in recycling activity in order to meet the Government's statutory recycling targets. 2005/06 is also a statutory target year and based upon information currently available to the Authority it is envisaged that the boroughs will be required to increase their recycling activity by a further 35,167 tonnes over their 2004/05 target levels, i.e. to a total of 187,060 tonnes (excluding hardcore). However, despite the increase in recycling by boroughs the total waste stream continues to rise and therefore an increase of 3% has been allowed in this projection to reflect a continuation of the underlying increase in the waste stream for 2005/06, i.e. an additional 28,900 tonnes.

5.4 **Compensation Review**

5.4.1 Base upon information received from LondonWaste Ltd the 2005/06 budget forecast assumes that LondonWaste Ltd will obtain a further improvement in the price it obtains for the sale of its electricity and that the incineration capacity of the Edmonton EfW facility will reduce in the period to the end of December 2005 whilst the WID Refurbishment works are being undertaken. Both have the effect of reducing LondonWaste Ltd's potential claim for this period. In the case of the expected reduction in incineration levels LondonWaste can only claim under this clause for NLWA tonnages of waste actually incinerated at the Edmonton EfW facility up to a maximum of 475,000 tonnes. During the calendar year 2005 incineration levels are not expected to exceed 410,000 tonnes. After December 2005 incineration levels are expected to return to pre-WID levels of up to 550,000 tonnes per annum. See also paragraph 5.14.13 below.

5.5 **Fridges and Freezers**

5.5.1 The budget forecast allows for the treatment and disposal of c. 58,000 appliances.

5.6 **Landfill Tax**

5.6.1 The standard rate of landfill tax is due to rise from £15 to £18 per tonne on 1 April 2005. The budget forecast allows for this increase.

5.6.2 The budget forecast continues to allow for a higher landfill tax claim from LondonWaste Ltd as a result of the increased tonnages of waste that will be sent to landfill during the refurbishment works at the Edmonton EfW facility. This is limited by a 'floor' of 475,000 tonnes below which the NLWA will not pay any additional landfill tax on tonnages sent to landfill when the incineration capacity falls below 475,000 tonnes (agreed by the Authority 1/10/03). After December 2005 incineration levels are expected to return to pre-WID levels of up to 550,000 tonnes per annum and the landfill tax claim should reduce to reflect this.

5.7. Legislative Review – Hazardous Waste (+ £1.668m)

5.7.1 The budget forecast allows for a potential claim by LondonWaste Ltd for the additional cost of disposing of hazardous waste. Assuming a price increase from £110 to £150 in July 2005, when the full impact of the Hazardous Waste Regulations come into effect, there could be an additional cost to the Authority of c. £1.668m in 2005/06. As indicated at paragraph 3.7.1 above the merit of the potential claim will need to be assessed and further advice will be provided at the Budget meeting in February.

5.8. Legislative Review – Edmonton Rating Revaluation (+ £0.047m)

5.8.1 LondonWaste Ltd has also notified the Authority of its intention to make a legislative review claim in respect of the Edmonton Rating Revaluation that will take effect on 1 April 2005. LondonWaste advise that Section 69 of the Local Government Act 2003 removed the power to prescribe rateable values by order. As a consequence, for the revaluation due on 1 April 2005 for Edmonton will be valued by the Valuation Office on a conventional commercial basis. LondonWaste Ltd advise that this will have the effect of significantly increasing the Edmonton rating valuation from 446,476 to 2,200,000 (provisional) and increase the annual charge from c. £0.204m to c. £1.030m. However, assuming transitional arrangements that normally apply in such circumstances the cost would rise to the new level over a period of 5 years; on this basis the potential claim in 2005/06 is estimated to be in the order of £0.047m.

5.8.2 At the time of writing the Authority has not had the opportunity to examine the merits of the potential claim. Advice will be provided at the Budget meeting in February.

5.9. Ashburton Grove Transfer Station/Hornsey Street Replacement

5.9.1 The 2005/06 budget forecast allows for the full year additional cost of operating the new waste transfer station at Hornsey Street. This has been based upon the original cost assumptions provided by LondonWaste Ltd. The new facility has now been operational for almost 5 months and officers are due to meet with LondonWaste Ltd to review the operations and to obtain an update on the additional costs of operating the new facility. Any change will be reported to the Authority in February.

5.10 Recycling Credits

5.10.1 The budget forecast allows for the Authority to fund a further significant stepped change in recycling activity next year, i.e. an additional 35,170 tonnes over 2004/05 projected tonnages, i.e. a total of 196,060 tonnes. The recycling credit payment is estimated to be £61.47 per tonne.

5.11 Dividend Income (LondonWaste Ltd)

5.11.1 No income is anticipated from this source.

5.12 Non-household Waste Charges

5.12.1 As previously proposed at the October meeting, the budget forecast assumes the continued use of the existing trade waste charging scheme and waste survey data as a basis for calculating non-household waste charges in 2005/06.

5.12.2 Based upon estimated non-household tonnages of 167,510 tonnes and a cost per tonne of £44.16 the total cost to boroughs in 2005/06 is currently estimated to be £7.397m. The cost for individual boroughs is estimated to be:-

	2005/06 Estimated Tonnes	2005/06 Estimated Cost £
Barnet	18,883	833,873
Camden	36,129	1,595,457
Enfield	13,806	609,673
Hackney	24,774	1,094,020
Haringey	23,298	1,028,840
Islington	28,534	1,260,061
Waltham Forest	22,086	975,318
	167,510	7,397,242

5.12.3 At the October meeting Members were advised that AEA Technology had completed an interim report advising of the results of its survey to quantify the waste generated by households and the waste composition across the seven constituent councils. The intention is to use this information to review the arrangements for determining the non-household charges in future years. Although the interim report indicated an average weight per household of 16 kgs per week wide variations between the data collected for some boroughs meant that further work was required before the Authority could begin to model alternative non-household charging arrangements for discussion with the constituent councils. AEAT is now near to completing this additional work and therefore it should be

possible to begin discussions with constituent boroughs in the near future. Nevertheless, it will not be possible to develop an alternative non-household charging arrangement which can be consulted upon and agreed in time for 2005/06.

5.13 Implementation of the Joint Waste Strategy

5.13.1 No allowance has been made for the potential capital cost of implementing the Joint Waste Strategy in 2005/06. This matter is to be considered by the Strategy Implementation Board on 6 December 2004.

5.14 Landfill Allowance Trading Scheme

5.14.1 The Landfill Allowance Trading Scheme (LATS) which is due to come in to effect on 1 April 2005 will restrict waste disposal authorities' use of landfill for the disposal of biodegradable municipal waste (BMW). BMW derives from both the household and non-household waste streams managed by the Authority. As a general rule each authority will be subject to progressively diminishing annual allowances for the landfilling of BMW. However, as previously reported the NLWA should find itself with a favourable trading position in the period until 2009/10 - the Authority's provisional allowances rise from 315,427 tonnes in 2005/06 to 360,596 in 2009/2010 – however, the allowances are due to reduce sharply to 240,183 tonnes by 2012/13 and to 168,064 tonnes by 2019/2020. In the period until 2009/10 the method adopted by the Government to determine landfill allowances will be of benefit to the NLWA and to those authorities that have invested in/make use of waste treatment facilities such as the Edmonton EfW facility or divert a significant proportion of their tonnage from landfill by recycling or composting. Where an authority's landfilled BMW tonnages exceed its allowances, the authority will have to either buy allowances from the market to cover the shortfall or pay penalties to the Government at £200 for each tonne of BMW that exceeds its allowances.

5.14.2 It is clear that LATS could have a very substantial financial impact in the coming years, particularly when the NLWA's allowances reduce sharply after 2009/10.

5.14.3 The first year of the scheme's operation will coincide with the refurbishment works that are being undertaken by LondonWaste Ltd to meet the requirements of the Waste Incineration Directive. As the incineration capacity of the Edmonton EfW facility is expected to reduce by some 25% in 2005 the first year of LATS could prove difficult for the Authority to achieve. After 2005/06, however, the Authority expects to be in a positive trading position that should enable it to sell surplus allowances. Ahead of the scheme implementation, however, the value of the allowances is unknown. In practice the value will be determined by market forces. In the early years of the scheme it is currently envisaged that demand, and therefore initial values, will be low as increased recycling and composting since 2001/02 will improve the diversion of biodegradable waste from landfill. Although values are likely to rise as allowance allocations reduce, it is also possible that values could fall once new treatment facilities became operational.

- 5.14.4 Although it is currently envisaged that there should be no direct financial impact on the Authority arising from LATS in 2005/06, what happens in relation to BMW next year does have financial implications for later years. This is because unused allowances may be 'banked' at the year-end and then used or sold in a later year. Every tonne of BMW that is landfilled next year will use an allowance that will then not be available for use or sale in subsequent years. As a consequence, in later years the Authority would be required to either incur additional expenditure because of the need to buy allowances or pay penalties, or suffer a loss of income. This has two main implications.
- 5.14.5 Firstly, as from April 2005, any extra diversion of BMW from landfill should produce an additional financial benefit to the Authority in subsequent years. The Authority may wish to consider whether there is scope to reward boroughs that reduce the BMW content of their waste stream.
- 5.14.6 Secondly, because of the potential cost implications in future years (including opportunity cost in the case of authorities with surplus allowances), all BMW sent to landfill could actually be more costly to the Authority than might first appear in the Authority's accounts. As a consequence, consideration will need to be given to what effect this should have, if any, on the charges that the boroughs should pay to the Authority for their collected non-household waste.
- 5.14.7 The 2005/06 budget forecast shown above only allows for non-household charges to increase by inflation plus a £3 per tonne increase in landfill tax. It does not allow for a further increase to cover potential LATS costs.
- 5.14.8 Where boroughs provide a non-household collection service the charges made are generally expected to cover the reasonable costs of collection and disposal. The Authority advises the boroughs of the non-household charges for the cost of disposal. The matter now for consideration is should the disposal charge include a proper apportionment of the expected costs arising from LATS (including opportunity cost as the Authority expects to have surplus allowances – at least in the early years). A LATS-related increase in non-household charges may well divert a proportion of this waste to the private sector (which remains outside LATS) and would have the effect of either reducing the need to buy allowances in the future or increase the surplus of allowances for future trading.
- 5.14.9 Although it is felt that the Authority's charges in principle should include an allowance for the costs (including opportunity costs) arising from LATS and properly attributable on a tonnage basis to the non-household waste stream, the difficulty is to determine in advance what these costs may be. It is known that the West London Waste Authority has been considering the merit of increasing its non-household charges by £40 per tonne from next April. The Western Riverside Waste Authority is also considering the possibility of an increase; although not quantified the current thinking in the absence of a clear picture of future markets, but the likelihood that there will be a surplus of allowances in year one of the scheme, is that a relatively small LATS-related increase would be justifiable. AEA Technology, the Authority's external technical consultant, has suggested a price in the

region of £15 in a 'perfect' market. The general view is that a nil increase seems unlikely to be justifiable.

- 5.14.10 Non-household tonnages in 2005/06 are currently estimated to in the order of 167,510 tonnes. Thus for every £1 increase there would be an additional income to the Authority £167,510 (assuming there was no reduction in tonnages).
- 5.14.11 Increasing the Authority's income from non-household charges next year to reflect LATS costs that may not arise until future years presents the Authority with the choice of planning to either:
- (i) earmark the additional resources to help mitigate costs in future years,
 - (ii) reduce the levy,
 - (iii) introduce a payment scheme to encourage boroughs to reduce the BMW content of their waste stream (household and non-household wastes),
 - (iv) a combination of one or more of the above.
- 5.14.12 Borough technical officers have been asked to consider the potential impact on their non-household collection services as these are judgements that the Authority is not well placed to make, especially as the position is likely to vary from one borough to another.
- 5.14.13 The Authority has the opportunity to require LondonWaste Ltd to incinerate all NLWA waste up to a maximum of 475,000 tonnes in order that the Company can claim the maximum subsidy under the Compensation Review claim. The subsidy is limited to a maximum 475,000 tonnes of NLWA waste incinerated each year. When the Hendon Waste Transfer Station management arrangement was originally agreed in December 1998 LondonWaste Ltd agreed to pay NLWA the avoided cost of transporting 75,000 tonnes of waste to Edmonton in order to maximise its Compensation Review Claim. As a consequence only 400,000 tonnes of the Authority's waste is actually incinerated at present but the Company is allowed to claim the maximum subsidy. This provides the Authority with an income of £3.60 per tonne and is currently worth about £0.300m to the Authority. When the new management arrangement was negotiated earlier this year LondonWaste was advised that in view of LATS this arrangement would need to end as it was necessary for the Authority to actually minimise its use of landfill. Officers are currently in discussions with the Company to examine the potential implications of this. This action has the potential to increase the Authority's surplus allowances by up to 75,000 tonnes. The 2005/06 budget forecast assumes that no income will be received in 2005/06.
- 5.14.14 The issues raised by LATS will be considered by the Waste Strategy Implementation Board and also the Member Working Group established to examine the strategic and policy issues that will need to be addressed and the procedures that will need to be put in place for the Authority to be able to trade in the coming year. Between now and the Budget meeting the Authority will also continue to consult with the boroughs on the opportunities presented by this proposal.

5.14.15 The February meeting of the Authority will include an update on LATS trading and the administrative arrangements that will need to be put in place from April 2005. The report will also deal with any impact of LATS-related costs that may be added to non-household charges in 2005/06. In the interim Members are invited to provide their initial comments on the proposals set in this section.

6. **Review of the Levy Arrangements**

6.1 Members will be aware that earlier this year the Government raised afresh the prospect of changing the default basis for apportioning the levy. Although some initial discussion between DEFRA and the Joint Waste Disposal Authorities took place in the Summer and reference has been made in the Clean Neighbourhood Consultation exercise to revise the recycling credit system to allow for the introduction of a tonnage-based levy, the Government has yet to consult on options for changing the default arrangement. There is therefore no prospect of a change in the default arrangements for apportioning the levy in 2005/06.

6.2 Nonetheless, in keeping with the practice of previous years, Members will be provided with details of possible alternative bases for apportioning the levy at the budget and levy meeting in February 2005.

7. **Conclusion**

7.1 On the basis of current information the third review indicates that the 2004/05 budget remains sufficiently robust to meet the cost of the Authority's waste disposal obligations in the current year. The Authority, however, is faced with the possibility of significant budget pressures in the year ahead. The budget forecast for 2005/06 currently indicates that the cost to boroughs is estimated to rise by £5.420m, i.e. an increase of 12.01% over the equivalent cost in 2004/05. The report draws attention to the impact of recycling activity on the residual waste stream and allows for the possible financial effect of new legislative review claims by LondonWaste Ltd. As these issues have yet to be finalised they have the potential to influence the final shape of the 2005/06 budget and levy.

7.2 This report has also discussed the merits of reviewing the Authority's charges for municipal commercial waste in the light of the statutory Landfill Allowance Trading Scheme which is due to come into effect on 1 April 2005. The report also raises the possibility of rewarding boroughs that take steps to reduce the level of biodegradable municipal waste from entering the waste stream.

7.3 Members will be aware that the Authority is not able to make a substitute levy and therefore in February it will be necessary for Members take decisions to ensure that the 2005/06 budget is sufficient to meet the Authority's statutory obligations in the year ahead. Members will be provided with further advice at the budget meeting in February.

8. **Comments of the Legal Adviser**

- 8.1 The report at paragraphs 5.7 and 5.8 outlines two potential claims from LondonWaste Ltd. In paragraph 5.14 there is an outline proposal for the recovery of costs from constituent boroughs and possible payments to them, the Legal Adviser has been instructed to look at the legal consequences of these matters with a view to incorporating this advice into the report to be put before the Authority at the February meeting.

Local Government Act 1972 - Section 100 as amended

Documents used in the preparation of this report:-

Reports to the Authority dated 11 February 2004, 7 July 2004 and 13 October 2004
2004/05 budgetary control and 2004/06 budget working papers

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